

Classroom Site Fund Update

Based on updated data, the projected FY 2006 Proposition 301 K-12 Classroom Site Fund (CSF) distribution will be \$376 million. In comparison, the FY 2005 distribution was \$296 million. The revised projection is \$22 million less our March estimate, after adjusting for unanticipated year-end distributions.

The potential \$22 million distribution difference is primarily due to the following factors: 1) state trust land earnings provided about \$15 million less than expected for FY 2005 (which reduced FY 2006 carry forward monies) and will generate an estimated \$16 million less than expected for FY 2006 and 2) ADE was required to transfer about \$6 million in prior year carry forward monies for Proposition 301 additional school days out of the CSF (where they had been deposited) and into ADE's Permanent State School Fund, which helps fund additional school days and other K-12 formula costs. (The state General Accounting Office originally instructed ADE to deposit the \$6 million into the CSF, but later reversed that decision.) These two factors are offset by \$15 million in higher than projected growth in Proposition 301 sales tax revenues for FY 2006. The March 2005 CSF estimate assumed 6.6% sales tax growth for FY 2006, whereas the revised estimate assumes 10.5% growth.

State Trust Land earnings can underperform either because of lower than expected inflation-adjusted investment returns from the State Treasurer (who invests monies from past trust land sales) or because recent buyers of state trust lands pay off their purchases early, which reduces the amount of interest paid into the CSF by the State Land Department. ("Early pay offs" increase the amount of land trust monies available for investment by the Treasurer, but those investments do not immediately generate cash to replace lost Land Department interest.) For FY 2005, the \$15 million shortfall in state trust land earnings for the CSF included a \$9.5 Treasurer shortfall and \$5.5 million Land Department shortfall.

ADE distributed 13 rather than 12 CSF payments for FY 2005 because enough CSF revenues existed to make 2 "back payments" for FY 2004 plus 11 (rather than 10) "current year" payments for FY 2006. (Cash flows into the CSF started off 2 months "late" when Proposition 301 programs began in FY 2002, requiring CSF "back payments" to be made every year since that time.) To the extent that schools did not spend their "13th payment" monies during FY 2005 (which is likely since they were received late in the year), they should remain available for use during FY 2006. Apart from those monies, schools are expected to receive about \$318 per pupil from the state CSF for FY 2006 under the revised figures. Of the \$318, \$35 is one-time in nature.

The JLBC Staff noted in the March 2005 memo on this topic that the original \$353 per pupil estimate did not include adjustments for contingencies "such as underperforming revenues, higher than expected enrollment growth, or monies being deposited too late into the CSF to be distributed in FY 2006... because current law does not make provision for such adjustments." It also noted that \$70 of the original \$353 amount was due to carryforward monies that should be viewed as one-time in nature.

Any lowering of CSF revenues reduces per pupil allocations out of the fund. The state is not required to offset lower than estimated CSF revenues pursuant to A.R.S. § 15-977(F).